

No. 15,645

United States Court of Appeals
For the Ninth Circuit

HAROLD M. KOCH, BESSIE KOCH, WIL-
LIAM L. KOCH, ROSE KOCH, REBECCA
KOCH ABEL, MAURICE P. KOCH, and
DAISY KOCH,

Appellants,

VS.

UNITED STATES OF AMERICA,

Appellee.

On Appeal from the United States District Court
for the Northern District of California.

APPELLEE'S BRIEF.

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Subject Index

	Page
Jurisdiction	1
Statement of the case	2
Summary of the argument	6
Argument	9
1. The instruction concerning the effect of the Commissioner of Internal Revenue's denial of the refund claim is not grounds for reversal	9
(a) Neither of appellants' counsel objected to the instruction when it was given by the court. They are precluded from now raising it for the first time	9
(b) Assuming that appellants may for the first time in this court inquire into the propriety of the instruction, the instruction does not constitute sufficient ground to reverse the jury's verdict	12
2. The direction of a verdict against Maurice P. Koch and Daisy Koch did not prejudice any of the appellants	14
(a) The partnership was not prejudiced	15
(b) Maurice P. Koch and Daisy Koch were not prejudiced	16
3. The court did not err in the instruction that the jury could disregard any of the activities of Maurice P. Koch as proof that the partnership was engaged in the business of financing motion pictures if it believed that in a particular transaction he was acting on his own behalf and not on behalf of the partnership	18
4. The court did not err in refusing to give the instructions proposed by appellants numbered 13 and 15	19
5. Argument of the appellee's counsel was not prejudicial misconduct	24
6. The court did not err in its rulings on admission of evidence	25

	Page
7. The jury verdict was not contrary to the weight of the evidence	27
8. The evidence warranted the jury verdict. The court correctly might have directed a verdict against the appellants and was generous to them in leaving the question to the jury. Accordingly, appellants have not been prejudiced by the jury verdict	29
(a) Maurice P. Koch was acting as a shareholder and director of two corporations and not on behalf of the partnership	29
(b) Ambassador Pictures Corporation and Producers Finance Corporation were not agents of the appellants	31
(c) The activity of financing motion picture ventures cannot be a trade or business within the meaning of the Internal Revenue laws	32
Conclusion	33

Table of Authorities Cited

Cases	Pages
Allen v. Matson Navigation Co. (9th Cir., April 7, 1958) ..	19
Ayers v. Watson, 137 U.S. 584, 601 (1902)	23
Buckeye Powder Company v. E. I. DuPont De Nemours, et al., 248 U.S. 55 (1918)	16, 17
Burnett v. Clark, 287 U.S. 410 (1932)	26, 30, 32
Carpenter v. Connecticut General Life Ins. Co., 68 F.2d 69 (10th Cir. 1933)	20
Commissioner v. Smith, 203 F.2d 310 (2d Cir. 1953), cert. denied 346 U.S. 816 (1953)	21, 23, 30, 32
Commissioner v. Stokes Estate, 200 F.2d 637 (3d Cir. 1953)	30
Dalton v. Bowers, 287 U.S. 404 (1932)	26, 30, 32
Freeman v. Churchill, 30 C.2d 453, 183 P.2d 4 (1947)	16
Friedman v. Delaney, 171 F.2d 269 (5th Cir. 1948)	23
Giblin v. Commissioner, 227 F.2d 692 (5th Cir. 1955)	21
Helvering v. Taylor, 293 U.S. 507 (1935)	14
Hickerson v. Commissioner, 229 F.2d 631 (2d Cir. 1956) ...	21, 33
Higgins v. Commissioner, 312 U.S. 212, 217 (1941)	27
Hutchinson v. Pacific Atlantic Steamship Co., 217 F.2d 384 (9th Cir. 1954)	11
Knight v. Russ, 77 Cal. 410, 414, 19 Pac. 698, 700 (1888)	25
Lloy v. Pacific Electric Ry. Co., 207 F.2d 662 (9th Cir. 1953)	10
Lynch v. Oregon Lumber Co., 108 F.2d 283, 286 (9th Cir. 1939)	11
Macartney v. Compagnie Generale Transatlantique (9th Cir. Feb. 28, 1958)	11
Maloney v. Spencer, 172 F.2d 638 (9th Cir. 1949)	21
Maroosis v. Smyth, 187 F.2d 228, 231-232 (9th Cir. 1951)	14
Moline Properties, Inc. v. Commissioner, 319 U.S. 436, 439 (1945)	31
National Carbide Corporation v. Commissioner, 336 U.S. 422, 437 (1949)	31

	Pages
Persons v. Gerlinger Carrier Corporation, 227 F.2d 337 (9th Cir. 1955)	10
Pokress v. Commissioner, 234 F.2d 146 (5th Cir. 1956) ...	23
Skarda v. Commissioner, 250 F.2d 429 (10th Cir. 1957)	26, 27, 28, 30
Towers v. Commissioner, 247 F.2d 233 (2d Cir. 1957), cert. denied 355 U.S. 914 (1958)	21, 33
Union Trust Company v. Woodrow Mfg. Co., 63 F.2d 602 (8th Cir. 1933)	16
United Press Associations v. Charles, 245 F.2d 21 (9th Cir. 1957)	11
United States v. Jones, 33 U.S. 399 (1834)	20
Van Dyke v. Commissioner, 63 F.2d 1020 (9th Cir. 1933) affirming 23 B.T.A. 946 (1931), affirmed 291 U.S. 642 (1933)	30
Wood Workers Tool Works v. Byrne, 191 F.2d 667, 676 (9th Cir. 1951)	11

Rules

Federal Rules of Civil Procedure, Rule 51	10
Rule 18(d) of the Rules of the United States Court of Ap- peals for the Ninth Circuit	10

Statutes

28 U.S.C., Section 1291 (1952)	2
28 U.S.C., Section 1346(a)(1) (1952)	1
Internal Revenue Code of 1939, Section 23(e)(2)	5

Miscellaneous

California Jury Instruction Civil 135 (4th Rev. Ed. 1956) ..	13
California Jury Instruction Civil 206-B (4th Rev. Ed. 1956)	13

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On Appeal from the United States District Court
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APPELLEE'S BRIEF.

JURISDICTION.

On July 5, 1955 in the United States District Court for the Northern District of California, Southern Division, the appellants filed an action for recovery of federal income taxes alleged to have been erroneously assessed and collected. Jurisdiction was invoked pursuant to 28 U.S.C. § 1346(a)(1) (1952). Trial by jury was demanded by the appellants, and the action was tried before the court and a jury on November 26, 27, 28 and 29. The jury returned a verdict in

favor of the appellee and on January 23, 1957 judgment was entered in favor of the appellee. A motion for new trial was filed and served on February 1, 1957, and denied on March 5, 1957. On April 18, 1957 the appellants filed a notice of appeal. Jurisdiction is invoked pursuant to 28 U.S.C. § 1291 (1952).

STATEMENT OF THE CASE.

Appellants are a copartnership engaged in the business of luggage manufacturing. (Exhibit 1.) On October 23, 1944 the partnership agreement was amended to permit the partnership to engage in the business of financing motion pictures through direct participation, stock investment or loans. Two of the factors necessitating an amendment were the provisions in the original agreement that no partner could remain away from the business 60 days and that all of the partners must devote all of their time to the business. (Exhibit 1, pages 2 and 3.)

In April, 1946 Beacon Pictures Corporation, a corporation, was formed to engage in the production of motion pictures. The partnership did not engage in the organization of that corporation. (R. 147-148.) This action is based upon an alleged loss of \$90,000 through loans to Beacon Pictures Corporation. The loans were made in the following manner:

On April 25, 1946 the partnership issued a check payable to Mr. David Sebastian in the amount of \$15,000.00. (R. 47-50.) \$10,000.00 of this amount was

a loan to the partnership of David Hersch and Sam Coslow to set up Beacon Pictures Corporation. The remaining \$5,000.00 was a loan to Hersch and David Sebastian for expenses in commencing production. (R. 50.) An additional \$2,500.00 was loaned to Hersch and Sebastian for the same purpose. (Exhibit 8, R. 53.) The loan of \$10,000.00 to Hersch and Coslow was to be repaid by Hersch and Coslow when the picture was completed and sold. (R. 52.) The partnership thereafter drew checks in the amount of \$50,000.00 (Exhibit 10-A, R. 55-56) and \$30,000.00 (Exhibit 13, R. 68-69) to the order of Sebastian. The partnership received notes from Beacon Pictures Corporation for these two loans of \$50,000.00 and \$30,000.00. (Exhibits 12, 14; R. 68-69.) The partnership advanced an additional \$20,000.00 to Beacon Pictures Corporation, which amount was returned. (Exhibit 18, R. 74-75.)

The picture was completed, distributed, and was a failure. The partnership obtained a judgment against Beacon Pictures Corporation for \$80,000.00 (R. 157) and filed a claim against the bankrupt estate of Beacon Pictures Corporation. Subsequently it was determined that the loans to Beacon Pictures Corporation were worthless.¹ This is the loss which is the basis of the appellants' claim for refund. In addition, the taxpayers claimed as a loss the \$15,000.00 originally loaned to Hersch and Sebastian (see above)

¹Appellants loaned \$97,500. Evidently \$7,500 of this represented loans made by Roy Haller (R. 277-279). This \$80,000 judgment against Beacon Pictures Corporation contained a \$5,000 claim of Roy Haller.

claiming that those loans were in fact made to Beacon Pictures Corporation.²

In addition to their isolated loan to Beacon Pictures Corporation, the appellants claim to have been engaged in the business of financing motion picture ventures. This claim of a business is based upon the following activity. Ambassador Productions, Inc. was formed and all shares of stock were issued to Maurice P. Koch. (R. 83.) This corporation purchased the rights to the book "Hill of the Hawk". (R. 93.)

A second corporation, Producers Finance Corporation, was formed in October, 1947. (R. 96.) Maurice P. Koch was president of that corporation from the moment of its inception. (R. 165.) As president of Producers Finance Corporation, Maurice P. Koch introduced Mr. Jack Chertok of Apex Film Corporation to the officers of the Pacific National Bank to secure a loan for Apex Film Corporation. (R. 174-175.) At this time, Apex Film Corporation had already been formed, and had made preparations to produce films. (R. 174.) Maurice P. Koch's only interest in this transaction was as a creditor of Apex Film Corporation. (R. 173-174.)

²In the complaint, the appellants alleged a \$90,000 loss. The appellee admitted this loss. In the course of the trial, the evidence disclosed that the loans were made to Hersch and Sebastian and Hersch and Coslow. The appellee moved the court to permit an amendment to the answer denying that the \$15,000 loss was suffered by the appellants. (R. 289-290.) This motion was denied. (R. 292.) Although the court failed to state the reason for this ruling, it was probably that since the court was directing a verdict as to the \$15,000 in dispute, there was no necessity for permitting an amendment to the answer in relation to that amount.

To further impress upon the jury that the appellants were in the business of financing motion picture ventures, there was testimony of numerous conversations, discussions, airplane journey and midnight phone calls by Maurice P. Koch. (See, for example, R. 202.) However, during much of this time, Maurice P. Koch was an officer and director of Producers Finance Corporation and Ambassador Pictures Corporation. (R. 167.)

The appellants filed income tax returns for the years 1945 and 1947. They thereafter amended these returns claiming a deductible loss for the year 1947 and a net operating loss carryback for the year 1945 arising out of the transaction involving Beacon Pictures Corporation. The claims for refund were denied upon the ground that that loss was a non-business bad debt. The appellants thereupon filed this action seeking refund of the tax paid.

In the complaint, the appellants also asserted that the loss was a loss arising out of a transaction entered into for profit within the meaning of Section 23(e) (2) of the Internal Revenue Code of 1939. Prior to trial counsel for the appellants agreed that this issue was being withdrawn from the action. Appellants state that no such stipulation was made. (See Appellants' Opening Brief, pages 58-59.) Unfortunately, the stipulation was not in writing. However, the instructions proposed by the appellants and the appellee, and the interrogatories submitted to the jury all omitted any reference to whether the transaction was in fact a transaction entered into for profit rather

than a debt. The conclusion is obvious that such a stipulation was made.

At the close of the evidence, the appellee moved (1) for a directed verdict as to all appellants and (2) to amend the answer to deny that Maurice P. Koch lost \$15,000 in addition to the \$75,000 lost by the partnership. The motion to amend was denied, and the motion for a directed verdict was granted against Maurice P. Koch and Daisy Koch for the \$15,000 which they claimed in addition to a share of the partnership loss. The jury then returned with a verdict that H. Koch and Sons was not regularly engaged in the business of financing motion picture ventures.

SUMMARY OF THE ARGUMENT.

1. (a) The appellants should not be permitted to allege error in the instruction that there is presumption that the determination by the Commissioner of Internal Revenue is correct and the appellants must overcome that presumption by a preponderance of the evidence. The appellants failed to object to the instruction when it was given. Therefore, they are precluded from challenging the instruction for the first time in this court.

(b) Assuming that the appellants may raise an objection to the instruction, the instruction was not erroneous. The instruction did not purport to give any weight as evidence to the Commissioner's presumption. The instruction stated that the appellants

had the burden of proving by a "preponderance of the evidence" that they were engaged in the trade or business of financing motion pictures. This did no more than state the burden placed upon a plaintiff in a civil action.

2. The directed verdict against Maurice P. Koch and Daisy Koch did not prejudice any of the appellants.

(a) The directed verdict did not prejudice the partnership. Maurice P. Koch testified that on all occasions he was acting on behalf of the partnership. (Appellants' Opening Brief, page 57.) None of the testimony of Maurice P. Koch was excluded. Thus, the jury considered all the testimony of Maurice P. Koch, in which he stated he was acting solely for the partnership, to determine whether or not the partnership was engaged in the business.

(b) Maurice P. Koch and Daisy Koch were not prejudiced by the directed verdict. Maurice P. Koch never claimed to have been acting for himself. He based his claim of a trade or business upon his identity with the partnership. Therefore, the directed verdict against Maurice P. Koch is immaterial since he is bound by the jury verdict that the partnership was not engaged in the business.

3. The court did not err in the instruction that the jury could disregard any of the activities of Maurice P. Koch where the jury believed he was acting on his own behalf and not on behalf of the partnership. Everything that Maurice P. Koch did, he did

in his own name. In fact, he advanced monies without the knowledge of the partnership. There was no evidence that the partnership acquiesced in all his activities. The ultimate issue must remain with the jury. The partnership agreement was only one of the factors they were warranted in considering to determine whether he was always acting for the partnership.

4. There was no error in the court's failure to give the three instructions requested by the appellants that in determining whether or not the appellants were engaged in the business of financing, the jury must consider all activity whether or not the transactions were actually concluded. The court permitted testimony of discussion, documents, telephone calls, all concerning activity where no proof was made that money was invested. In its charge, the court then stated to the jury that it could consider all of the time and effort devoted by the appellants. There was no restriction that actual financing must have occurred.

5. The argument to the jury by appellee's counsel concerning the activity of the Commissioner of Internal Revenue was not improper. Counsel was merely commenting upon the fact stated in the appellants' pleading. As such, it is proper comment to the jury.

6. The rulings of the court in relation to evidence received or excluded were proper. Documents excluded had no foundation and had no relevance to the trade or business of the partnership.

7. The jury's verdict is supported by the evidence. The existence of a partnership agreement alone cannot transcend any factual inquiry into whether or not the appellants actually did engage in a business. The jury observed the witnesses testify to the amount of time and effort expended in financing motion picture ventures. The trial court was liberal in permitting the jury to consider testimony of activity of separate and distinct corporate entities. The issue was a factual one and should be left to the jury to decide whether or not the appellants were engaged in the trade or business of financing motion picture ventures.

8. The court could have properly directed a verdict against appellants, but was generous in permitting the issue to be decided by the jury.

ARGUMENT.

1. THE INSTRUCTION CONCERNING THE EFFECT OF THE COMMISSIONER OF INTERNAL REVENUE'S DENIAL OF THE REFUND CLAIM IS NOT GROUNDS FOR REVERSAL.

(a) Neither of appellants' counsel objected to the instruction when it was given by the court. They are precluded from now raising it for the first time.

When the court concluded instructing the jury, counsel were given an opportunity to raise objections. (R. 306.) Counsel for the appellants excepted to instructions given and also took exception to the court's failure to give instructions. At no time did they raise

any objection to the instruction to which they now complain.

Rule 51 of the Federal Rules of Civil Procedure provides in part:

“No party may assign as error the giving or the failure to give an instruction unless he objects thereto before the jury retires to consider its verdict, stating distinctly the matter to which he objects and the grounds of his objection.”

Fed. R. Civ. P. 51.

And, Rule 18(d) of this court provides in part:

“When the error alleged is to the charge of the court, the specification shall set out the part referred to totidem verbis, whether it be in instructions given or in instructions refused, together with the grounds of the objections urged at the trial.”

Appellants' counsel failed to object as provided by Rule 51 of the Federal Rules of Civil Procedure, and accordingly are unable to comply with the requirements of Rule 18(d) of the Rules of the United States Court of Appeals for the Ninth Circuit.

This court has long required compliance with Rule 51 of the Federal Rules of Civil Procedure. A failure to object to the instruction when given precludes raising any objection to that instruction at the time of appeal.

Persons v. Gerlinger Carrier Corp., 227 F.2d 337 (9 Cir. 1955);

Lloy v. Pacific Electric Railway Co., 207 F.2d 662 (9 Cir. 1953);

Wood Workers Tool Works v. Byrne, 191 F.2d 667, 676 (9 Cir. 1951);

Lynch v. Oregon Lumber Company, 108 F.2d 283, 286 (9 Cir. 1939).

See also:

Macartney v. Compagnie Generale Transatlantique, 9 Cir. Feb. 28, 1958;

United Press Associations v. Charles, 245 F.2d 21 (9 Cir. 1957).

In *Macartney v. Compagnie Generale Transatlantique*, decided February 28, 1958, this court stated,

“Our view of the propriety of the court’s action in giving supplementary instructions in open court in the absence of counsel and any objection by such counsel makes it unnecessary to rest our affirmance upon the nature and content of the supplementary instructions.”

In a footnote to that statement, this court stated,

“In *Hutchinson v. Pacific Atlantic Steamship Company*, 217 F.2d 384 (1954), this court said: ‘As to the alleged error of the court in giving certain instructions: Appellant made no objection to the instruction she now complains of. In fact, she informed the court she had no objections. She should not now be heard to complain.’ [page 386.]”

Thus, as recently as February 28, 1958, the court reaffirmed its position that in order to raise an objection to an instruction, the appellant must have made formal objection to the instruction in the trial court.

- (b) Assuming that appellants may for the first time in this court inquire into the propriety of the instruction, the instruction does not constitute sufficient ground to reverse the jury's verdict.

The charge to which the appellants now complain was as follows:

“The burden of proof in this case is upon the plaintiffs to prove by a preponderance of evidence that the loan by plaintiffs to the Beacon Pictures Corporation was a loan made to plaintiffs' regular trade or business. There is a presumption that the determination by the Commissioner of Internal Revenue that the plaintiffs were not engaged in the trade or business of financing motion pictures is correct. The burden is upon the plaintiff to overcome the presumption of the correctness of the Commissioner's determination by proving by a preponderance of evidence that they were engaged in the trade or business of financing motion pictures.” (R. 301.)

The court then went on to discuss what it meant by evidence and a preponderance of evidence saying:

“By a preponderance of evidence is meant such evidence as when weighed with that opposed to it has more convincing force, and from which it results that the greater probability is in favor of the party upon which the burden rests. Preponderance of evidence means not the greater number of witnesses but the greater weight, probability, quality and a convincing effect of the evidence and proof offered by the party holding the affirmative as compared with any opposing evidence. If the scales of proof hang evenly the verdict should be against the party who has the burden of proof.

In determining whether any issue has been proven by a preponderance of evidence you should consider all of the evidence bearing either way upon the question, regardless of who produced it. A party is entitled to the same benefit from evidence that favors his cause or defense when produced by his adversary as when produced by himself.” (R. 302.)

The court did not instruct the jury that the presumption was to be considered as evidence in the case.

If appellants thought there was any error in this instruction they could easily have called it to the court’s attention. Instead they would now set aside a four-day trial on the basis of such an afterthought and on an alleged ground which obviously did not appear to them to be objectionable or prejudicial at the time the jury was charged. Appellants did not request explanation of the instruction as given. Instead, they remained mute.

In any event, the jury was not instructed that the presumption was to be given evidentiary weight, and the instruction did not convey that impression to them.³

³A comparison of the instruction given by the court with instructions given by California courts in certain cases where a presumption does carry evidentiary weight will indicate this. For example, the inference of *res ipsa loquitur* is evidence to be considered by the jury. The jury is therefore charged: “An inference arises that the proximate cause of the occurrence was some negligent conduct on the part of the defendant. That inference itself is a form of evidence, and if none other exists tending to overthrow it . . .” California Jury Instruction Civil 206-B (4th Rev. Ed. 1956) . . . Similarly, in California there is a presumption that every person acts free of contributory negligence. Therefore, the jury is instructed as follows: “At the outset of the trial, each party was entitled to the presumption of law that

The trial court was clearly correct in instructing the jury as to burden of proof and preponderance of the evidence. In a refund suit it has repeatedly been held that the burden is on the taxpayer to establish his right to recover and the amount of the refund.

Helvering v. Taylor, 393 U.S. 507 (1935);

Maroosis v. Smyth, 187 F.2d 228, 231-232 (9th Cir.), cert. denied 324 U.S. 814 (1951).

2. THE DIRECTION OF A VERDICT AGAINST MAURICE P. KOCH AND DAISY KOCH INDIVIDUALLY DID NOT PREJUDICE ANY OF THE APPELLANTS.

The complaint sought recovery for taxes paid because of an alleged loss in the amount of \$15,000 individually on behalf of Maurice P. Koch and Daisy Koch. This \$15,000 allegedly represented loans by Maurice P. Koch to Beacon Pictures Corporation in excess of his proportionate share of the partnership loan. The court directed a verdict as to this amount. (R. 292.) The record warranted this ruling on any of the following grounds:

(1) These were not loans to Beacon Pictures Corporation but loans to David Sebastian;

(2) There was insufficient proof that these loans were made by Maurice P. Koch and were not, in fact, loans of the partnership; or

every person takes ordinary care of his own concerns and that he obeys the law. These presumptions are a form of a prima facie evidence and will support findings in accordance therewith . . .” California Jury Instruction Civil 135 (4th Rev. Ed. 1956). These are instructions which tell the jury to give evidentiary weight to a presumption. The instruction given by the court in this action was not similar to these instructions and did not have the same effect.

(3) Maurice P. Koch never claimed to have been in the trade or business of financing motion pictures apart from his activities in the partnership.

Whatever the basis for the ruling, it is immaterial since no prejudice resulted to the appellants Maurice P. Koch and Daisy Koch or to the partnership H. Koch and Sons.

(a) The partnership was not prejudiced.

Maurice P. Koch was never acting on his own behalf. All of his activities were on behalf of the partnership. (R. 25, Appellants' Opening Brief 25, 33.) Although the court directed a verdict against Maurice P. Koch and Daisy Koch individually, the jury was permitted to consider all the activities of Maurice P. Koch in furtherance of the partnership business. The jury was instructed:

“Taxpayers may act through employees, agents and other persons, firms and corporations appointed by such taxpayers, and the acts of such employees, agents, or other persons, firms or corporations appointed by the taxpayer are in contemplation of law the act of the taxpayer. Thus, in considering the activities of the taxpayers in the instant case with relationship to the conduct, if any, of the business or enterprises, you are required to consider that the act of any such employees, agents, persons, firms or corporations appointed by them are in fact the acts and activities of the taxpayers.

“The authorized act or acts of any one partner of H. Koch and Sons in connection with the

partnership business or activities, are in contemplation of law the act or acts and activities of all of the partners." (R. 301.)

Thus, the jury was instructed to consider all the activities of Maurice P. Koch where it believed he was acting in furtherance of partnership interests in determining whether the partnership was engaged in the business of financing motion picture ventures. The partnership conducted its activities in the business of motion picture financing through the activities of Maurice P. Koch. Since the jury considered all of Maurice P. Koch's testimony, the partnership had the benefit of all evidence which was introduced.

(b) **Maurice P. Koch and Daisy Koch were not prejudiced.**

All of Maurice P. Koch's activity was on behalf of the partnership. He never purported to act for his own interests. Therefore, any finding on the partnership's business would be a finding upon the business of Maurice P. Koch individually.

Although the granting of a directed verdict may be error, if the jury verdict reaches the same result as the directed verdict, the parties can claim no prejudice.

Buckeye Powder Company v. E. I. DuPont De Nemours, et al., 248 U.S. 55 (1918);

Freeman v. Churchill, 30 C.2d 453, 183 P.2d 4 (1947);

Union Trust Co. v. Woodrow Mfg. Co., 63 F.2d 602 (8 Cir. 1933).

In *Buckeye Powder Company v. E. I. DuPont De Nemours, et al.*, 248 U.S. 55 (1918), the trial court directed a verdict in favor of certain defendants. The jury then returned a verdict in favor of the remaining defendants. The Supreme Court stated that since the liability of the defendant who was favored by the directed verdict was predicated upon the liability of the defendant who received the jury verdict, all defendants were exonerated by the jury verdict. The court held that in such a situation, an erroneous directed verdict does no harm.

The situation here is identical. Whether Maurice P. Koch was in the business of financing motion picture ventures depended upon whether the partnership of H. Koch and Sons was in the business of financing motion picture ventures. This result is necessitated by the appellants' position that Maurice P. Koch never acted on his own behalf, but on behalf of the partnership. Therefore, by its verdict concerning the partnership, the jury found that Maurice P. Koch was not in the business of financing motion pictures. If the court did not grant the directed verdict and deny recovery for the alleged \$15,000 individual loss, the jury verdict would have reached the same result. Therefore, any error in directing a verdict against Maurice P. Koch and Daisy Koch was not prejudicial.

3. THE COURT DID NOT ERR IN INSTRUCTING THE JURY THAT IT COULD DISREGARD ANY OF THE ACTIVITIES OF MAURICE P. KOCH AS PROOF THAT THE PARTNERSHIP WAS ENGAGED IN THE BUSINESS OF FINANCING MOTION PICTURES IF IT BELIEVED THAT IN A PARTICULAR TRANSACTION HE WAS ACTING ON HIS OWN BEHALF AND NOT ON BEHALF OF THE PARTNERSHIP.

The court instructed as follows:

“If you believe that Maurice P. Koch used his own money in any transaction and was acting therein in his own behalf and not on behalf of H. Koch and Sons, that transaction cannot be considered by you in determining whether the partnership of H. Koch and Sons was engaged in the business of financing motion pictures.”
(R. 302.)

The appellants do not contend that this instruction does not properly state the law. (Appellant's Opening Brief, pages 31, 34.) Their complaint is that the instruction does not give sufficient weight to the testimony of Maurice P. Koch.

Maurice P. Koch testified that on every occasion he was acting on behalf of the partnership. Appellants allege error in the instruction that the jury was not compelled to believe him. The only basis for holding this instruction error is for the court to say that a jury is compelled to believe the testimony of an interested witness.

The jurors were instructed that they were the exclusive judge of the credibility of the witnesses. (R. 302.) The court further instructed them in the manner in which this credibility was to be determined. (R. 303-304.) If the jurors are not permitted to de-

termine the credibility of Maurice P. Koch, then they are compelled to accept as true the uncontradicted testimony of every witness. Such is not the law. See *Allen v. Matson Navigation Company*, 9th Cir., April 7, 1958.

Although Maurice P. Koch stated that he always acted on behalf of the partnership, other inferences may be drawn from the facts. For example, of the \$25,000 loaned by Producers Finance Corporation to Ambassador Pictures Corporation for purchase of the book "Hill of the Hawk", \$17,000 was repaid personally to Maurice P. Koch. (R. 177.) On cross-examination Maurice P. Koch divulged that the funds loaned were personal funds, that the partnership was short of money, and that the loan was never reflected on the partnership books. (R. 161.) Certainly the inference was permissible that the transaction was a personal transaction, and the appellee was entitled to an instruction which would permit the jury to draw that inference. In addition, the appellee impeached Maurice P. Koch in relation to his attempts to collect \$80,000 from Beacon Pictures Corporation. (R. 156-158.) In view of this impeachment, the jury should be permitted to evaluate the testimony of Maurice P. Koch to determine whether he was telling the truth.

4. THE COURT DID NOT ERR IN REFUSING TO GIVE THE INSTRUCTIONS PROPOSED BY APPELLANTS NUMBERED 13 AND 15.

The instruction which apparently was appellants' proposed instruction number 13 stated:

“That in determining whether or not H. Koch and Sons was engaged in the business of financing motion picture ventures, you must consider, among other things, the amount of time and effort expended in that direction and such time and effort, if any, must be considered by you whether or not an actual venture was concluded.” (R. 25-26.)

The instruction which is apparently referred to as appellants' instruction number 15 was as follows:

“That in considering the question as to whether or not H. Koch and Sons devoted substantial time to the financing of motion picture ventures, you are required to consider all of their activities relating to that purpose, and all activities and efforts actually expended in attempting to negotiate for and in attempting to enter into financial transactions relative to the business of financing motion picture ventures must be considered by you upon this issue whether the same were concluded or not.” (R. 26.)

These instructions are confusing. The phrase “whether . . . an actual venture was concluded” is ambiguous and indefinite. There is no explanation in the instruction of how a venture is “concluded”. Therefore, the court could not give these instructions, since to do so would be error.

United States v. Jones, 33 U.S. 399 (1834);
Carpenter v. Connecticut General Life Ins. Co.,
 68 F.2d 69 (10th Cir. 1933).

But, assuming the instructions were not ambiguous, there was no error in refusing to include them in the

charge to the jury. Whether or not the activity constitutes a trade or business is a question of fact.

Maloney v. Spencer, 172 F.2d 638 (9th Cir. 1949).

To constitute a trade or business it must be shown that the activity was extensive, that it was regularly carried on, and that it constituted a major portion of the time, energy and effort of those who claim it as a trade or business.

Towers v. Commissioner, 247 F.2d 233, 235 (2nd Cir. 1957), cert. denied 355 U.S. 914 (1958);

Hickerson v. Commissioner, 229 F.2d 631 (2nd Cir. 1956);

Giblin v. Commissioner, 227 F.2d 692 (5th Cir. 1955);

Commissioner v. Stokes Estate, 200 F.2d 639 (3rd Cir. 1953).

The court instructed the jury:

“In determining that question you should consider all of the evidence which has been admitted in the case. The question of whether the debt is one the loss from the worthlessness of which is incurred in the taxpayer’s trade or business is a question of fact in each particular case. The statute does not give a definition for the word ‘business.’ Accordingly, in determining whether H. Koch & Sons was regularly engaged in the business of financing motion picture ventures you should consider the word ‘business’ to have its ordinary, common and accepted meaning. A taxpayer may engage in or regularly conduct one or several businesses at the same time. The amount

of time as well as the proportionate amount of capital devoted to a particular business are each factors among other factors to be considered in determining whether or not one is regularly engaged in a particular business.

“If a taxpayer regularly and continuously participates in business ventures in which he is not only financially interested but to which he devotes a substantial part of his time, such activities may make such ventures a trade or business of the taxpayer. Isolated or infrequent transactions of a taxpayer in any field do not constitute a trade or business within the meaning of the Internal Revenue Code.

“In determining whether an activity of a taxpayer is a trade or business you should consider among other things how extensive was the activity, the financial investment therein, whether it was regularly carried on, and whether the activity occupied a substantial portion of the time, energy and effort of the taxpayer.”

This was a proper statement of the applicable legal principles. The court advised the jury that the amount of time spent was a factor to be considered in determining whether the partnership was engaged in a trade or business. The jury was further advised that it was to consider whether the activity was regularly carried on and whether it occupied a substantial portion of the time, energy and effort of the partnership. Under this instruction, the jury was advised to consider all activities of the taxpayer, regardless of whether financing was accomplished.

And this was the nature of the evidence which the court permitted to go to the jury. Appellants, over

objection by the appellee, were permitted to introduce evidence relating to numerous phone calls, conversations, and documents relating to activities of the appellants in matters where no financing was ever accomplished.

Evidently the appellants complain that the court did not specifically instruct the jury that the appellants could be in the business of financing "whether or not an actual venture was concluded." (R. 26.) Although the court did not use the appellants' language, the import of its charge to the jury was that the jury should consider all activity of the taxpayers whether or not financing was concluded. Nothing further was required. "A judge is not bound to adopt the categorical language which counsel choose to put into his mouth. Nothing could be more misleading. If the case is fairly put to the jury, it is all that can reasonably be asked."

Ayers v. Watson, 137 U.S. 584, 601 (1902).

But even if this court determines that the instructions did not permit the jury to consider activities where financing was not actually accomplished, the appellants were not entitled to such an instruction. Where the business is that of lending money, the important issue is whether or not the taxpayer had actually loaned money.

Commissioner v. Smith, 203 F.2d 310 (2nd Cir. 1953), cert. denied 346 U.S. 816;

Pokress v. Commissioner, 234 F.2d 146 (5th Cir. 1956);

Friedman v. Delaney, 171 F.2d 269 (5th Cir. 1948).

Thus, whether loans were made was a factor to be considered in determining whether the taxpayers in the above cases were in the business of making loans. Here, therefore, whether any financing was actually done should be a factor to be considered in determining whether the appellants were engaged in the business of financing motion pictures. Accordingly, the appellants were not entitled to the instructions which advised the jury that whether or not actual financing was done was immaterial.

**5. ARGUMENT OF THE APPELLEE'S COUNSEL WAS
NOT PREJUDICIAL MISCONDUCT.**

Counsel for the appellee stated to the jury:

“You see, the plaintiff already had one crack at this case. He filed his claim for refund with the Commissioner of Internal Revenue and the Commissioner denied it.”

Upon objection by counsel for appellant, the court instructed the jury: “This is the first time the case has been tried and counsel was correct. A claim has been filed”. Counsel for the appellee then stated that the “matter had been presented to the Commissioner of Internal Revenue.” (R. 344.) Thus, the jury was not told that the case had been tried previously.

The jury was told that the defendant, through the Commissioner, believed this was a non-business bad debt. This was the fundamental issue in the action. The appellants claimed a business loss, and the appellee claimed it was a non-business bad debt. Appel-

lee's counsel merely informed the jury of the appellee's contentions.

In the complaint, appellants alleged: "The Commissioner of Internal Revenue, through the office of the Regional Commissioner of Internal Revenue, notified plaintiff on September 10, 1954 that said \$9,375 chargeable loss was a 1947 loss but that in his opinion the loss was a non-business bad debt and was therefore a capital loss and thus was deductible by petitioner in 1947 only in the amount of \$1,000." (Supp. R. 386.) The complaint was replete with similar statements. (Supp. R. 388, 390, 392-93, 394, 396, 398, 400, 402, 404, 406, 408-09, 411, and 413.) Appellee's counsels' remarks were merely stating what the appellants had alleged in the complaint. In *Knight v. Russ*, 77 Cal. 410, 19 Pac. 698 (1888), plaintiff's counsel read parts of the complaint to the jury. The Supreme Court of California there stated: "And if in the progress of the argument, counsel desires . . . to further call the attention of jury to the facts alleged, there can so far as we can see, be no impropriety in doing so."

Knight v. Russ, 77 Cal. 410, 414, 19 Pac. 698, 700 (1888).

6. THE COURT DID NOT ERR IN ITS RULINGS ON ADMISSION OF EVIDENCE.

Plaintiffs offered an agreement between one Sam Coslow and the United Artists Corporation. (Exh. 5, Appellants' Opening Brief, Appendix D.) It con-

tained no reference to the appellants. (R. 213.) The only purpose of the agreement was to show the activity of other persons. Appellants' counsel stated: "It is part of the overall picture, to show the contribution of each person toward the entire pot that makes the independent picture." (R. 211-212.) The agreement did not relate to any activity of the appellants, and therefore, had no bearing upon whether the appellants were in the business of financing motion pictures. In any event, there was sufficient testimony of the existence of the agreement. (R. 45-46.) Thus, appellants' counsel were not prejudiced by the failure to admit the document.

Plaintiffs' offers of Exhibits 19, 24, 26, and 29 were refused by the court. These exhibits all related to activity of third persons and Ambassador Pictures Corporation. Ambassador Pictures Corporation was an independent entity, whose activities are not the activities of the appellants.

Dalton v. Bowers, 287 U.S. 404 (1932);

Burnett v. Clark, 287 U.S. 410 (1932);

Skarda v. Commissioner of Internal Revenue,
250 F.2d 429 (10th Cir. 1957).

The exhibits, therefore, are not relevant to show the activities of the appellants.

But, in any event, whether or not the documents are relevant, the appellants were not prejudiced by their exclusion. The documents were not offered for the truth of the statements contained in them, but were offered to prove the fact of the documents themselves—they were offered as proof of activity. With

the offer of each document, Maurice P. Koch testified that he had authorized or directed the preparation of the document as part of his activity. Although the document was not admitted in evidence, the very fact of the activity was in evidence by testimony of Maurice P. Koch.

**7. THE JURY VERDICT WAS NOT CONTRARY TO THE
WEIGHT OF THE EVIDENCE.**

The issue was whether the appellants were in a trade or business within the meaning of the Internal Revenue laws. The appellants alleged that they were in the business of financing motion picture ventures. Whether or not the activity constituted a trade or business was a question of fact.

Higgins v. Commissioner, 312 U.S. 212, 217 (1941).

Here, the appellants amended their partnership agreement to provide that they would be in the business of financing motion picture ventures. Appellants contend that the existence of the partnership agreement compelled the finding that they were in fact engaged in the business of financing motion pictures. However, it would seem that the existence, or non-existence of an agreement to engage in a business is merely a factor to be considered in determining whether the parties are actually engaged in the business.

In *Skarda v. Commissioner*, 250 F.2d 429 (10 Cir. 1957), the taxpayers were a partnership which engaged in various activities. One of the activities was the publication of newspapers. Subsequently, the

partners became the sole owners of a corporation which undertook the publishing business. However, there were no meetings of stockholders, no by-laws, no election of officers, no minute books, no corporate stock, and no property was formally transferred by the partnership to the corporation. Thereafter, the partnership made loans to the corporation which became worthless. The partnership claimed business deductions for these losses. The partnership contended that since it was the sole shareholder of the corporation, and that the corporation was merely organized to carry on business of the partnership and had not complied with the laws of the State relative to the formation of corporations, the losses were in fact business losses of the partnership.

The Court of Appeals for the Tenth Circuit denied this contention. It held that the losses had no relation to any business of the partnership. Thus, the fact that the partnership had agreed to engage in the publishing business was immaterial without further proof of actual publication.⁴

The appellants here demanded a trial by jury upon the issue of whether or not they were engaged in the business of financing motion picture ventures. The issue for the jury was whether evidence introduced by appellants showed sufficient activity to constitute a trade or business. The jury determined that it did not. This verdict should not be set aside.

⁴Although in the *Skarda* case, the court did not state that the partnership agreement was in writing, this would appear to be immaterial. Whether the agreement is in writing or oral is not relevant if the existence of the agreement is accepted.

8. THE EVIDENCE WARRANTED THE JURY VERDICT. THE COURT CORRECTLY MIGHT HAVE DIRECTED A VERDICT AGAINST THE APPELLANTS AND WAS GENEROUS TO THEM IN LEAVING THE QUESTION TO THE JURY. ACCORDINGLY, APPELLANTS HAVE NOT BEEN PREJUDICED BY THE JURY VERDICT.

(a) The means by which the partnership attempted to place itself in the business of financing motion pictures was through the activity of Maurice P. Koch. Although Maurice P. Koch was a partner in H. Koch and Sons, the partnership cannot adopt his activity to establish the business of financing motion pictures.

Maurice P. Koch was also an officer and director of Ambassador Pictures Corporation and Producers Finance Corporation. He testified extensively to negotiations for the purchase of "Hill of the Hawk" by Ambassador Pictures Corporation. However, financing the purchase of "Hill of the Hawk" for Ambassador Pictures Corporation was not done by Maurice P. Koch on behalf of the partnership, but was done by Maurice P. Koch on behalf of Producers Finance Corporation. (R. 167.) It was Producers Finance Corporation which loaned \$25,000.00 to Ambassador Pictures Corporation for purchase of "Hill of the Hawk", not Maurice P. Koch, or the partnership. (R. 176-177, Defendants' Exhibit "I".) In all the dealings by Maurice P. Koch in relation to the purchase of "Hill of the Hawk", he was not acting as a partner in H. Koch and Sons, but he was acting as the shareholder, officer and director of Ambassador Pictures, Inc. (R. 164-165.) Through his own testimony, it is evident that Maurice P. Koch was acting in his capacity as shareholder and director

of Ambassador Pictures Corporation and Producers Finance Corporation.

Further evidence that the loan to Ambassador Pictures Corporation was made by Producers Finance Corporation and not the partnership was the check to Ambassador Pictures. The maker of the check was Producers Finance Corporation. (Defendants' Exhibit I, R. 176-177.) The financing, therefore, could not have been by the partnership.

The corporation is regarded as an entity distinct from its shareholders, directors or officers. Relying upon this principle, the Supreme Court of the United States has held that the business of the corporation is not the business of the shareholder, officer or director.

Dalton v. Bowers, 287 U.S. 404 (1932);

Burnett v. Clarke, 287 U.S. 410 (1932).

See also:

Skarda v. Commissioner, 250 F.2d 429 (10th Cir. 1957);

Commissioner v. Smith, 203 F.2d 310 (2nd Cir. 1953), cert. denied 346 U.S. 816;

Commissioner v. Stokes Estate, 200 F.2d 637 (3rd Cir. 1953);

Van Dyke v. Commissioner, 63 F.2d 1020 (9th Cir. 1933), affirming 23 B.T.A. 946 (1931), affirmed 291 U.S. 642 (1933).

The major portion of Maurice P. Koch's activity was devoted to his activities as shareholder and director of Ambassador Pictures Corporation and Producers Finance Corporation. (R. 167.) This activity cannot be considered in determining whether H. Koch

and Sons was engaged in the business of financing motion pictures. If the activity is excluded, there was not sufficient evidence of activity by the partnership to sustain a finding that they were in the business of financing motion picture ventures.

(b) It is appellants' contention that although Maurice P. Koch may have been acting on behalf of Ambassador Pictures Corporation and Producers Finance Corporation, these corporations were the agents of the appellants. [See Appellants' Opening Brief 51-54 and proposed Instruction No. 9 (R. 24) which was given by the Court (R. 301).] To be considered an agent, the corporate business purpose must be carrying on the duties of an agent.

National Carbide Corporation v. Commissioner,
336 U.S. 422, 437 (1949).

Here, the corporations were not formed to act as agents, but were formed for the specific purpose of producing motion pictures (R. 82) and financing motion pictures (R. 95). The activities of these corporations cannot be ascribed to the partnership.

National Carbide Corporation v. Commissioner,
336 U.S. 422 (1949);

Moline Properties, Inc. v. Commissioner, 319
U.S. 436, 439 (1945).

If the activities of Ambassador Pictures Corporation and Producers Finance Corporation are excluded, there was not sufficient evidence of activity by the appellants to sustain a finding that they were in the business of financing motion picture ventures.

(c) The activity of financing motion picture ventures cannot be a trade or business within the meaning of the Internal Revenue laws.

The business of the corporation cannot be the business of the shareholders or directors. A taxpayer associated with many corporations cannot rely on the activities of the organization, but must establish his own activity apart from the organization's to prove a trade or business.

Dalton v. Bowers, 287 U.S. 404 (1932) ;

Burnett v. Clarke, 287 U.S. 410 (1932).

In *Commissioner v. Smith*, 203 F.2d 310 (2nd Cir. 1953), cert. denied, 346 U.S. 816 (1953), the Second Circuit refused to recognize investment management and other forms of financing as a trade or business.

This Court has taken a similar position. In *Ada v. Van Dyke*, 23 B.T.A. 1953, the taxpayer was engaged in development and promotion of town sites. The taxpayers financed the development of the town sites, utility companies and other forms of municipal improvements. The loss in question resulted from a loan to a corporation to promote the development of land sites and utilities. The Board of Tax Appeals held that the loss did not result from a trade or business. This Court affirmed, 63 F.2d 1020 (1933), citing *Burnett v. Clarke*, *supra*, and *Dalton v. Bowers*, *supra*. The judgment was affirmed by the Supreme Court of the United States, 291 U.S. 642 (1933). There, the investment and loans were made with the purpose of promoting, financing and organizing the utility companies and real estate improvement land.

See also:

Hickerson v. Commissioner, 229 F.2d 631 (2nd Cir. 1956);

Towers v. Commissioner, 247 F.2d 233, 235 (2nd Cir. 1957), cert. denied 355 U.S. 914 (1958).

The import of these decisions is that one who is instrumental in the formation of corporations and suffers a loss through a loan to one of the corporations, has not suffered a loss arising out of a trade or business. If these cases are to be followed, the activity of the appellants was not a trade or business.

CONCLUSION.

The judgment should be affirmed.

Dated, April 23, 1958.

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